

CALIFORNIA INFRASTRUCTURE AND ECONOMIC DEVELOPMENT BANK (I-BANK)

STAFF REPORT

SUMMARY

Staff requests the Board appoint five firms to serve as financial advisor to the I-Bank in relation to existing and future bond and loan programs and future bond issuances, and to authorize a contract with each firm for a term not to exceed 36 months, in each case in an amount not to exceed \$25,000. Staff further requests the authority to enter into one or more engagement letters with any of the pool of appointed firms, during the period of any such contract, for future bond issuance related services, subject to the limitation that such services shall be paid solely from bond proceeds, and that payment shall be conditioned upon the issuance of bonds.

BACKGROUND

The I-Bank currently has contracted with four financial advisory firms to provide financial assistance with I-Bank programs and bond issuances. These three-year contracts will expire on June 30, 2010. The need for independent financial advisory services related to the I-Bank's bond and infrastructure loan programs is ongoing due to the bond and loan workload of the I-Bank.

A Request for Qualifications (RFQ) was issued on April 22, 2010 for the I-Bank staff to select one or more firms to provide financial advisory services relating to the following scope of services:

- A. Financial analysis and assistance with structuring complex Infrastructure State Revolving Fund Program loans.
- B. Assistance with the issuance of bonds and/or post bond services for revolving loan programs such as the I-Bank's ISRF Program, the California State Water Resources Control Board Clean Water Revolving Loan Fund and other State revolving loan program bonds issued by the I-Bank.
- C. Assistance with the issuance of bonds and/or post-bond work related to I-Bank's State School Fund Apportionment Lease Revenue Bond Program.
- D. Assistance with the issuance of bonds and/or post-bond work related to any other I-Bank Bond Financing Programs (excluding pooled bond issuances¹).
- E. Assistance with financial advisory work related to the development of innovative and new economic development bond and/or State or Federal financing programs that facilitate the development of public development facilities or economic development facilities within the State.

¹ On August 25, 2009, the I-Bank Board established a list of financial advisors specifically for pooled bond issuances undertaken by the I-Bank. The pooled bond financial advisor list is still active and this RFQ did not include financial advisory work related to such pooled-bond issuances.

- F. Other debt and financial management matters or special projects as requested by I-Bank.

The RFQ cited examples of typical financial advisory tasks that include, but are not limited to, the following:

- Perform credit analysis and assist with structuring a variety of credit types and repayment streams for individual credits to be included in the revolving loan program bond issuances.
- Participate in meetings and conference calls with I-Bank staff, other State staff, applicants, borrowers, and/or other financing team members as needed.
- Analyze the cost benefits of different bond structuring and pricing options including, but not limited to, fixed rate versus variable rate bonds, insured versus uninsured bonds, callable versus non-callable bonds, and par versus discounted bonds.
- Participate in all bond pricing discussions. Based on direction from the I-Bank staff, provide data on market comparables and different indices that can be used in pricing discussions.
- Assist I-Bank staff in rating agency and/or bond insurer presentations or investor meetings related to a particular financing.
- Participate in bond document review and due diligence sessions. Coordinate with I-Bank staff and counsel to ensure compliance with federal tax law.
- Participate in reviewing the underwriter's quantitative analysis related to the bond sizing, structure and flow of funds.
- Assist I-Bank staff in reviewing the underwriter's proposed allocation of the bonds.
- Review and provide input on the preliminary and final bond official statements.
- Participate in post-financing review that includes a report addressing how the I-Bank's bonds priced relative to market indices, comparables and any goals established prior to sale.
- Assist I-Bank staff in reviewing and/or analyzing post-financing issues that may arise.

The RFQ contemplated that one or more firms will be selected. Any firm entering into an agreement with the I-Bank may be requested to provide services when it is determined that the firm is best suited to provide the services required. That determination will be based on a combination of all of the following:

- The availability of the firm to provide the requested services, which determination will take into account any client conflicts of interest the firm may have;

- The suitability of the firm to provide the requested services, which determination will take into account the Firm's experience for which services are being sought; and
- The hourly rate charged by each firm.

The RFQ was sent to all 49 firms on the State Treasurer's Office (STO) list of financial advisors approved for transactions undertaken by the STO, and the RFQ was also posted on the I-Bank's website at www.ibank.ca.gov. No questions were received from potential applicants by the April 29, 2010 deadline date. The following twelve firms responded by the May 5, 2010 due date:

1. Backstrom McCarley Berry & Company
2. Capitol Public Finance
3. Fieldman, Rolapp & Associates
4. First Southwest Company
5. Gardner, Underwood & Bacon LLC
6. KNN Public Finance (KNN)
7. Lamont Financial Services Corporation (Lamont)
8. MF Whipple & Associates
9. Public Financial Management (PFM)
10. Public Resources Advisory Group (PRAG)
11. Sequoia Financial Group LLC (Sequoia)
12. Urban Futures Inc.

ANALYSIS

A review committee comprised of I-Bank management evaluated each of the twelve proposals to ensure each firm met the minimum qualifications specified in the RFQ. The review committee determined that each firm submitting a proposal met the minimum qualifications.

Additionally, the committee evaluated the RFQ responses relative to each firm's ability to perform the selected scope of services, including information regarding the qualifications and experience of the firm and its personnel relative to revolving loan and bond financings, California state and local government and public school financings experience, as well as the firm's commitment to the State, its proposed rate of compensation and the overall quality of the responses. Based on this evaluation, the review committee recommends the selection of the following firms:

- KNN
- Lamont
- PFM
- PRAG
- Sequoia

The review committee concluded that having a choice of firms will enable the I-Bank to make firm selections based upon firm staffing availability and expertise. Continuing

past practice, a firm will only be paid for work the firm is requested to perform, and for work acceptably performed.

Three of the proposed firms are currently financial advisors to the I-Bank, Lamont, KNN and PFM. I-Bank staff have had good experiences working with each of these three firms during the term of the prior contract. I-Bank staff has had satisfactory experience working directly with principals of PRAG and Sequoia in the context of I-Bank conduit bond issuances.

The firms collectively have extensive experience and capabilities in planning, structuring, and executing a myriad of State and local municipal bonds, including:

- Voter-approved debt such as general obligation and registered voter special tax bonds;
- Revolving loan program bonds and pooled bond financings;
- Lease financings including certificates of participation and lease revenue bonds;
- Revenue bonds and installment sales certificates of participation;
- Tax allocation bonds and other forms of redevelopment finance;
- Assessment, special tax and Mello-Roos bonds;
- Judgment and pension bonds, tobacco-securitization bonds, insurance bonds and other hybrid security structures;
- Advance and current refundings;
- Fixed, variable-rate, multi-modal, and synthetic securities;
- Taxable municipal bonds;
- Short-term note financings; and,
- Long-term strategic planning and other types of municipal consulting.

Below are some brief highlights of the relevant experience of all five firms as described in the responses to the RFQ:

KNN

- Local Government Finance. During the past five years, the firm has provided financial advisory services on 109 local government municipal bond issues (not including schools) throughout California that involved tax allocation, lease revenue and enterprise revenue bond financings totaling over \$7.5 billion. The firm represented numerous municipalities participating in U.S. Environmental Protection Agency funded programs for clean water and drinking water. The firm's main clients are small to medium sized local governments that are infrequent issuers of debt similar to many ISRF Program borrowers.
- School Finance. The firm completed 191 long term primary and secondary education (K-14) school district financings totaling \$14.1 billion over the last five years. The firm served as financial advisor on the three inaugural I-Bank State School Fund Apportionment Lease Revenue Bond Program issues in 2005, a refunding in 2008, as well as the most recent King City Joint Union High School District issue.

- California Government Finance. The firm served as financial advisor on 37 transactions for the State of California with a total par amount of approximately \$9.75 billion over the last five years. KNN currently serves as financial advisor to the State Public Works Board in connection with its Lease Revenue Bond Program as well as the California State University System.
- Thomson Reuters ranked KNN among the decade's top 10 financial advisory firm nationally based upon par amount despite the firm's exclusive focus on California financings.

Lamont

- State Revolving Funds. The firm has extensive knowledge of the ISRF Program, having served as a financial advisor to the I-Bank since 1996. Lamont assisted with the development and implementation of the ISRF Program and issuance of the 2004, 2005, and 2008 ISRF Revenue Bonds. Lamont has also assisted with the design, development and implementation of SRF programs for 9 other states and serves as the financial advisor to five major state issuers of clean water and drinking water SRF programs.
- Local Government Finance. The firm has assisted California cities with the issuance of electric system revenue COPs, lease revenue bonds and wastewater system revenue COPs.
- California Government Finance. Lamont completed financial advisory assignments for financings totaling \$35.5 billion in California alone on numerous types of complex and unique bond issuances. The firm has extensive experience with other State agencies, including: the State Water Resources Control Board; the California Energy Commission; State Public Works Board; the Golden State Tobacco Securitization Corporation; the Economic Recovery Bond Committee; the Department of Transportation; Department of Corrections; and, the Department of General Services.

PFM

- Large nationwide firm that in 2009 provided financial advisory services to 832 bond transactions totaling over \$51 billion.
- State Revolving Funds. Since 2000, the firm has served as the primary financial advisor to U.S. EPA funded water and wastewater revolving funds (SRFs) in 14 of 27 states who leverage their SRF programs and several who are in the exploratory phase of leveraging. During this period, the firm assisted clients to issue 133 SRF related financings totaling a par amount of \$15.5 billion.
- Local Government Finance. Since 2005, PFM has assisted in 29 local government tax allocation bond issues totaling 1.2 billion, served as financial advisor for 28 lease revenue and leaseback Certificates of Participation (COP) transactions in California representing 1.7 billion of par value and completed 767 water, sewer and gas transactions between 2000-2009 for a total par value of 43.9 billion. PFM has advised on Tax Exempt Commercial Paper advising on 20 transactions for a total of \$2.3 billion nationwide since 2005.
- The firm has completed over 100 Build American Bond issues since the passage of the American Recovery and Reinvestment Act of 2009.

PRAG

- PRAG is the top-ranked financial advisory firm in California for 7 of the past 10 years, including 2009. The firm has completed more than 250 transactions totaling over \$155 billion over the last 190 years in California (Thomson Reuters).
- State Revolving Funds. In 2002, PRAG professionals assisted the I-Bank to issue bonds for the inaugural leveraging of the State Water Resources Control Board Clean Water SRF.
- Local Government Finance. In the last five years, the firm has served as financial advisor on 77 local government bond sales totaling \$17.1 billion.
- School Finance. PRAG's lead professional was the underwriter on the I-Bank's 2005 State School Fund Apportionment Lease Revenue bonds, as well as lease financings for school districts in San Diego, Los Angeles and Val Verde (Riverside County).
- California Government Finance. PRAG was hired as first financial advisor to the State Treasurer over 20 years ago and continues to serve as financial advisor on the State's fixed rate general obligation bond program.

Sequoia

- Sequoia is certified as a small business by the California Department of General Service. Newly created financial advisory firm with two principals that have over 50 years of combined financial advisory, rating agency and bond underwriting experience at other firms.
- State Revolving Fund. One of Sequoia's principals assisted in the creation of the *Criteria, Priority and Guidelines* for the ISRF Program, and was the underwriter on the I-Bank's ISRF Program Bonds, Series 2004. One of the firm's principals underwrote bonds issued on behalf of the State Water Resources Control Board for the Clean Water State Revolving Fund participated as an underwriter for \$63 million Florida State Infrastructure Bank revenue bonds.
- Local Government Finance. The firm recently closed \$16.6 million in water revenue bonds for Garden Grove Public Financing Authority.
- School Finance. The firm currently serves a financial advisor to California School Finance Authority and Sweetwater Union High School District.

Fees. All firms submitted proposals for varying hourly rates, ranging from the hourly rates applicable to work performed by managing directors/partners/principals to subordinate staff such as senior vice president, vice president, senior managing consultant, consultant, assistant vice president, associate and analyst. The final fee proposals for the selected firms for the hourly rate to be paid to a firm's highest paid representative are as follows:

Firm	Highest Hourly Fee
KNN	\$300
Lamont	\$275 first contract year \$285 second and third contract years
PFM	\$300
PRAG	\$300
Sequoia	\$275

The initial fee proposal from KNN and PRAG included a maximum hourly rate higher than \$300 per hour, but in recognition of the competitiveness of the fee proposals received from other firms, following negotiation with I-Bank staff, these two firms reduced their maximum hourly rate proposal to \$300.

Contracts. Staff proposes to enter into a three-year contract for \$25,000 with each appointed firm detailing the scope of responsibilities as well as the method of compensation. The RFQ stated that the I-Bank reserved the right to extend the term of any contract entered into as a result of the selections made pursuant to the RFQ for up to two additional years, subject to the satisfactory negotiation of terms acceptable to both parties. Staff recommends that the Executive Director be delegated the authority to make firm selections for financial advisory assignments.

Engagement Letters. Staff also proposes that these five firms be approved as a pool of financial advisory firms eligible for appointment by the Executive Director to serve as the I-Bank's financial advisor in relation to specific future bond transactions. Any such appointment will be based on the firm's expertise in providing the type of financial advisory services required by the specific bond transaction, and on cost of services. Upon appointment, the firm will enter into an engagement letter with the I-Bank, which shall provide that any compensation for the bond transaction related services will be solely from bond proceeds, and not pursuant to the existing contract between the firm and the I-Bank.

Application of Public Contract Code and Government Code. Government Code Section 63087 provides that any agreements entered into by the I-Bank in connection with the sale of bonds² is exempt from Public Contract Code Section 10295 and Sections 10335 to 10382, inclusive.

Government Code section 63086 authorizes engaging consultants in connection with the issuance of bonds and payment of those consultants from bond proceeds. Financial advisory services related to a bond issuance will be pursuant to an engagement letter, and shall be payable from bond proceeds. Financial advisory services not payable from bond proceeds will be engaged pursuant to a standard State consulting services contract.

² "Bonds" is defined in Government Code Section 63010(e) as "bonds, including structured, senior, and subordinated bonds or other securities; loans; notes, including bond, revenue, tax or grant anticipation notes; commercial paper; floating rate and variable maturity securities; and any other evidences of indebtedness or ownership, including certificates of participation or beneficial interest, asset-backed certificates, or lease-purchase or installment purchase agreements, whether taxable or excludable from gross income for federal income taxation purposes."

RECOMMENDATION

Staff recommends approval of Resolution 10-22 appointing the following five firms:

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Firm	Highest Hourly Fee
KNN Public Finance	\$300
Lamont Financial Services Corporation	\$275 first contract year \$285 second and third contract years
Public Financial Management	\$300
Public Resources Advisory Group	\$300
Sequoia Financial Group LLC	\$275

to serve as financial advisor to the I-Bank in relation to existing and future bond and loan programs and future bond issuances, and to authorize a contract with each firm for a term not to exceed 36 months, in each case in an amount not to exceed \$25,000, and in each case providing for compensation at not greater than the hourly rates as shown above. Staff further recommends that, for the period of these contracts, these five firms constitute a pool of financial advisors from which the Executive Director may appoint one or more firms to provide bond issuance-related services for future bond transactions, subject to the limitation that such services shall be provided pursuant to an engagement letter and paid for solely from bond proceeds, and that payment shall be conditioned upon the issuance of bonds. It is further recommended that each contract and engagement letter provide for reimbursement of the types of costs specified in the firms' responses to the RFQ or as otherwise reasonably approved by the I-Bank contract manager.

The term of each of these appointments or contracts is as stated above unless otherwise rescinded or extended by the Board.